

ST 02-32

Tax Type: Sales Tax

Issue: Gross Receipts

Unreported/Underreported Receipts (Fraud Application)

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS**

**THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS**

v.

**ABC, Inc.,
Taxpayer**

No. 02-ST-0000

IBT: 0000-0000

NTL: 00 00000000000000

**Charles E. McClellan
Administrative Law Judge**

RECOMMENDATION FOR DECISION

Appearances: John D. Alshuler, Special Assistant Attorneys General, for the Department of Revenue; Ubi O. O'Neal for ABC, Inc.

Synopsis:

This matter arose from a protest filed by the taxpayer on December 11, 2001 to a Notice of Tax Liability issued to ABC, Inc. ("taxpayer"), by the Department on November 28, 2001 for taxes assessed under the Retailers' Occupation Tax Act ("ROTA") 35 ILCS 120/1, *et seq.*, and related taxes. The issue is whether the taxpayer reported the correct amount of gross receipts from its sales of used cars and paid the proper amount of tax incurred on the sale of those cars. An evidentiary hearing was held on August 26, 2002. I recommend that the fraud penalty be canceled and that as so adjusted, the Notice of Tax Liability should be made final.

Findings of Fact:

1. The Department conducted an audit of the taxpayer's records for the period July 1, 1998 through November 30, 2000. Dept. Ex. No. 1.
2. At the conclusion of the audit, the Department prepared a Form SC-10-K Audit Correction and/or Determination of Tax Due ("corrected return"). *Id.*
3. On November 28, 2001, the Department issued a Notice of Tax Liability to the taxpayer assessing tax due. *Id.*

Conclusions of Law:

The ROTA requires every taxpayer to report to the Department the total amount of gross receipts on forms prescribed by the Department. 35 ILCS 120/3. The statute requires the Department to examine these returns and to issue notices of tax liability if it determines additional taxes to be due. Specifically, the statute provides as follows:

As soon as practicable after any return is filed, the Department shall examine such return and shall, if necessary, correct such return according to its best judgment and information.* * * In the event that the return is corrected for any reason other than a mathematical error, any return so corrected by the Department shall be prima facie correct and shall be prima facie evidence of the correctness of the amount of tax due, as shown therein. * *

* In making a correction of transaction by transaction, monthly or quarterly returns covering a period of 6 months or more, it shall be permissible for the Department to show a single corrected return figure for any given 6-month period.

If the tax computed upon the basis of the gross receipts as fixed by the Department is greater than the amount of tax due under the return or returns as filed, the Department shall (or if the tax or any part thereof that is admitted to be due by a return or returns, whether filed on time or not, is

not paid, the Department may) issue the taxpayer a notice of tax liability for the amount of tax claimed by the Department to be due, together with a penalty in an amount determined in accordance with Section 3-3 of the Uniform Penalty and Interest Act. 35 ILCS 735/3-3. Provided, that if the incorrectness of any return or returns as determined by the Department is due to negligence or fraud, said penalty shall be in an amount determined in accordance with Section 3-5 or Section 3-6 of the Uniform Penalty and Interest Act, 35 ILCS 735/3-5 or 735/3-6 as the case may be. 35 ILCS 120/4.

In the instant case, the Department examined the tax returns filed by the taxpayer for the audit periods. At the conclusion of the audit, the Department determined that the gross receipts of the taxpayer's business during the audit periods were greater than the amounts reported on the tax returns it filed. Accordingly, it prepared a corrected return calculating the deficiency and it assessed penalties, including a fraud penalty. On November 28, 2001, it issued Notice of Tax Liability 00 00000000000000 to the taxpayer.

Dept. Ex. No. 1

It is well established that a corrected return as prepared by the Department is deemed prima facie correct. *Masini v. Dept. of Revenue*, 60 Ill.App.3d 11, 14, 376 N.E.2d 324 (1st Dist.1978). At the hearing in this case, the Department established its prima facie case by introducing the corrected return into evidence. The burden then shifted to the taxpayer to overcome the Department's prima facie case. *Anderson v. Dept. of Finance*, 370 Ill. 225, 18 N.E.2d 206 (1938); *Masini v. Dept. of Revenue*, 60 Ill.App.3d at 14, 376 N.E.2d 325. 35 ILCS 120/4

"In order to overcome the presumption of validity attached to the Department's corrected returns, (the taxpayer) must produce competent evidence identified with their books and records and showing that the Department's returns are incorrect." *Masini*,

supra, 60 Ill.App.3d at 15; *Copilevitz v. Dept. of Revenue*, 41 Ill.2d 154, 242 N.E.2d 205 (1968); *Dupage Liquor Store, Inc. v. McKibbin*, 383 Ill.276, 48 N.E.2d 926 (1943). *Howard Worthington, Inc. v. Department of Revenue*, 96 Ill.App.3d 1132, 421 N.E.2d 1030 (2nd Dist. 1981).

In this case, the Department's *prima facie* case was established when the corrected return was entered into evidence under the certificate of the Director of Revenue. The burden then shifted to the taxpayer to overcome the Department's *prima facie* case.

The taxpayer's attorney appeared at the hearing but he did not offer any oral testimony by or on behalf of the taxpayer. He did offer what appears to be a copy of an unsigned letter. Taxpayer Ex. No. 1. The letter was entered into the record. However, it was offered with no foundation and it does not contain any information relevant to the Department's audit or to the deficiency or penalties assessed. Therefore, it was not persuasive. In sum, the taxpayer failed to produce any competent evidence identified with its books or records to overcome the Department's *prima facie* case.

Before this matter can be concluded, however two matters must be addressed. The first matter is the fraud penalty assessed by the Department. The second matter is a discrepancy between the tax periods and assessments as listed on the corrected return and the Notice of Tax Liability.

First, considering the fraud penalty, for the years at issue, if the Department alleges that an underpayment of tax is due to fraud, the statute provides a penalty to be assessed equal to 50% of the tax deficiency assessed by the Department. 35 ILCS 735/3-6. When the fraud penalty has been assessed, the burden of proof as to the fraud issue is

on the Department. *Brown Specialty Co. v. Allphin*, 75 Ill.App.3d 845, 394 N.E.2d 659 (3rd Dist. 1979) (The Department must provide clear and convincing evidence of fraud when fraud is asserted under the Retailers' Occupation Tax Act.) In this case, the Department did not offer clear and convincing evidence that the deficiency assessed is due to fraud. Therefore, the fraud penalty must be canceled.

Next, considering the discrepancies between the Notice of Tax Liability and the corrected return, the discrepancies are demonstrated in detail in the following table.

	Corrected return	Notice of Tax Liability
Audit period	7/98-4/01	7/98-11/00
Tax due	\$31,149	\$26,568
Late filing penalty	118	99
Late payment penalty	7,271	
Fraud penalty	15,575	13,284
Interest	0	6,952
Total	\$54,113	\$46,903

The statute allows the taxpayer 60 days after the date of the Notice of Tax Liability to file a protest to the assessment shown on the Notice of Tax Liability. 35 ILCS 120/5. It does not give the taxpayer the opportunity to protest the amount of tax and penalties shown on the corrected return. Therefore, the only tax deficiency at issue at an evidentiary hearing on a protest is the amount of tax and penalty shown on the Notice of Tax Liability. In this case, the amount of tax and late filing and late payment penalties are limited to the amounts shown on the Notice of Tax Liability.

Therefore, I recommend that the Notice of Tax Liability be amended to cancel the fraud penalty, and that as so corrected it be made final.

ENTER: September 30, 2002

**Charles E. McClellan
Administrative Law Judge**